



Wisconsin Defense Counsel

Defending Individuals And Businesses In Civil Litigation

**Written Comments for Senate Bill 9
Wisconsin Defense Counsel
(Formerly the Civil Trial Counsel of Wisconsin)
Andrew Cook**

February 5, 2009
Senate Committee on Judiciary, Corrections, Insurance,
Campaign Finance Reform, and Housing

Introduction

The Wisconsin Defense Counsel (WDC), (formerly the Civil Trial Counsel of Wisconsin (CTCW)) is a statewide organization of attorneys dedicated to the defense of Wisconsin citizens and businesses, the maintenance of an equitable civil justice system, and the education of its members. WDC appreciates the opportunity to provide these written comments to Senate Bill 9 (SB 9), providing a tort cause of action for intentional misrepresentation in a residential real estate transaction.

While SB 9 is narrowly drafted, WDC opposes the bill for the following reasons:

- Buyers already have statutory and contractual remedies. Therefore, there is no need to add a tort cause of action and punitive damages.
- Adding a tort claim and punitive damages will create an incentive for plaintiffs to file lawsuits as a means to extract money from sellers in cases where no fraud or misrepresentation has occurred.
- It will lead to the erosion of the well-established economic loss doctrine which seeks to preserve the distinction between contracts and torts.

Before discussing the merits of SB 9, however, it is important to provide a discussion of the Wisconsin Supreme Court's decision leading to the proposed legislation.

Wisconsin Supreme Court's Decision

In *Below v. Norton*, 208 WI 77, 310 Wis.2d 713, 751 N.W.2d 351, the Wisconsin Supreme Court held (4-3) that the economic loss doctrine bars common-law tort claims for intentional misrepresentation in real estate transactions.

In *Below*, a home purchaser brought a tort claim for intentional misrepresentation for a defect of the home that was not disclosed in the seller's property condition report. The Wisconsin Supreme Court ruled that the "economic loss doctrine" barred the purchaser's tort claim for intentional misrepresentation. (The economic loss doctrine is a judicially created doctrine which seeks to preserve the distinction between a contract and tort.)

Writing for the majority, Justice Patrick Crooks ruled that because the purchaser's alleged damage—the house's inadequate value—was an economic value, the economic loss doctrine barred a common-law tort claim for intentional misrepresentation.

In reaching its decision, the majority reiterated that the purchaser had other remedies. For example, the court noted that the purchaser could sue under Wis. Stat. § 100.18, which protects purchasers from a seller's false representations in the sale of real estate. The Supreme Court noted that the court of appeals had reversed the lower court and remanded the case to the trial court to allow the buyer to prove her statutory claims.

The court also declined to address whether the economic loss doctrine bars claims under Wis. Stat. § 943.20(1)(d) because the record before the lower court was unclear as to why the claim was dismissed. The Supreme Court remanded the case back to the trial court instructing the lower court to clearly state its decision as to the second statutory claim.

The court further noted that, in addition to statutory remedies, the purchaser had a potential contractual remedy. According to the court:

...if the Nortons [the sellers] knew about the defect with the sewer line and failed to disclose the defect, as required by these statutes, then the Nortons may very well have breached the contract's terms. As a result, in addition to her pending Wis. Stat. § 100.18 claim, Below might normally have been in a position to pursue a breach of contract claim against the Nortons for which contractual remedies would have been available.

The court ruled, however, that the purchaser failed to allege a breach of contract claim in her original complaint, and then failed to properly serve the parties when she amended her complaint. Therefore, the contract claim was not before the court in this case.

The dissenting opinion argued that the economic loss doctrine should not apply to home purchases because: 1) such purchases are not made between commercial parties, 2) a residential real estate transaction is not a contract for a product, and 3) residential real estate transactions are protected by neither manufacturer warranties nor the Uniform Commercial Code.

Senate Bill 9 – Adding a Tort Cause of Action for Intentional Misrepresentation

Senate Bill 9, if enacted, would amend Wis. Chap. 895 by adding a tort cause of action for an intentional misrepresentation made by the seller of real estate. Senate Bill 9 would give purchasers the ability to recoup not only the economic value of the home, but also punitive damages. (Statutory and contractual remedies do not allow punitive damages, but as mentioned above, do provide for attorneys' fees and costs.)

While SB 9 is narrowly drafted, if enacted, the bill would lead to an erosion of the economic loss doctrine. As noted in the Wisconsin Supreme Court's opinion, the economic loss doctrine is a well-established doctrine that has been applied in similar cases. The purpose of the economic loss doctrine is to preserve the distinction between a contract and a tort. This bill would undo that distinction.

Moreover, erosion of the economic loss doctrine is a real negative for Wisconsin's "business climate" at a time that we least need to discourage business retention, expansion and/or attraction in Wisconsin.

Last, as repeatedly mentioned by the Supreme Court, buyers already have statutory and contractual remedies for intentional misrepresentation of the sale of residential real estate. In fact, SB 9 recognizes the fact that there are already other remedies. (Section 1(2) of the bill states, "In addition to any other remedies available under law...") Thus, it is not clear why a buyer should receive punitive damages when other remedies already exist which make the buyer whole. Furthermore, WDC is concerned that SB 9 will incentivize plaintiffs to file a tort claim as a way to extract money in cases where no fraud or misrepresentation occurred.

Based on the foregoing, the Wisconsin Defense Counsel has serious reservations with SB 9 and therefore opposes the bill.

TESTIMONY

SENATE BILL 9

Senate Committee on Judiciary, Corrections, Insurance, Campaign Finance Reform, and Housing

2/5/09

Madam Chair and members of the committee, thank you for the opportunity to provide testimony in support of Senate Bill 9, legislation that Senator Erpenbach and I introduced to correct a problem in state law aimed at protecting home buyers who are victims of fraud.

As a result of a decision handed down by the Wisconsin Supreme Court last summer, home buyers lost their legal right to seek recourse against home sellers who defraud them during the purchase and sale of a home by knowingly failing to disclose a defect.

The court's decision in *Below v Norton* left a large void in the protections previously available to Wisconsin home buyers.

Senate Bill 9 restores the important provision of state law that allows victims of fraud when purchasing a home to seek legal redress in our courts that was eliminated under the Supreme Court's decision.

Senate Bill 9 enjoys broad support among those in the industry who help Wisconsin citizens both buy and sell homes and those people and organizations whose aim it is to protect consumers including Wisconsin Association For Justice and the Wisconsin Association of Home Inspectors and the Wisconsin Realtors Association.

With the housing market the way it is, making sure sellers are held accountable for the condition of the property they are selling is essential. Imagine if you are a family that has just made the biggest purchase of your life and that purchase turns into a nightmare because of a lie. This bill would restore balance to the law and give homebuyers some piece of mind as well as the needed legal option of being able to seek justice through our courts.

Thank you.



Memorandum

To: Members, Senate Judiciary, Corrections, Insurance, Campaign Finance Reform & Housing

From: Michael Theo, Vice President of Legal and Public Affairs
Tom Larson, Director of Regulatory and Legislative Affairs

Date: February 4, 2009

Re: Intentional Misrepresentations in Residential Real Estate Transactions (SB 9/AB 6)

The Wisconsin REALTORS® Association (WRA) encourages you to support SB 9/AB 6, which would restore the legal remedies available to buyers who are harmed by intentional misrepresentations made by sellers in residential real estate transactions.

Background

In residential real estate transactions, the seller is required by Wis. Stat. Chapter 709 to make property condition disclosures to the buyer in a real estate condition report (RECR). Up until now, sellers who misrepresented or concealed the condition of the home often were sued for intentional misrepresentation because the buyer could recover compensatory damages and punitive damages and could file suit based upon when the damage was discovered instead of when the deception occurred.

However, in Below v. Norton, the Wisconsin Supreme Court held that common law intentional misrepresentation claims are not valid in residential and noncommercial real estate transactions. See Below, 2008 WI 77, ¶41, 751 N.W.2d 351, 360-61 (2008). Rather, parties to a real estate transaction must look to the contract and the statutes to determine what, if any, remedies are available for misrepresentations. See *id.* at 361, ¶42. In other words, even if a buyer is able to prove that the seller made a misrepresentation, the buyer generally will be unable to collect punitive damages and have a difficult time rescinding the offer to purchase or the sale itself unless the contract specifically provides for such remedies.

Proposed Legislation

SB 9/AB 6 would restore the legal remedies that were available to homebuyers prior to the Below v. Norton case. Specifically, the legislation would allow homebuyers who are harmed by intentional misrepresentations made by the seller to sue for both compensatory and punitive damages.

Without the threat of punitive awards, the consequences for sellers who lie will typically be limited to compensatory damages to correct the defect the seller lied about or concealed. If the worst a seller could face would be to pay for the defect that they should have paid to fix in the first place, then sellers may decide against making truthful property condition disclosures. Since many buyers may be reluctant to sue because of the costs, time and burden of proving the case, particularly if the amount involved is only a few thousand dollars, sellers may conclude it is worth the risk to conceal defects and mislead buyers because they stand a decent chance of getting away with it.

By restoring the legal remedies available to homebuyers who are harmed by intentional misrepresentations made by a seller, the proposed legislation would:

- Promote full seller disclosure of property defects of which the seller is aware in residential real estate transactions because sellers are the ones most familiar with their homes, in keeping with Wisconsin public policy and Wis. Stat. ch. 709.
- Provide buyers who receive a seller's RECR with greater confidence that the information they receive from the seller is complete and accurate.
- Provide buyers who are harmed by a seller's intentional misrepresentations made with adequate legal remedies to efficiently and adequately compensate them for their losses.

We strongly urge you to support SB 9/AB 6. Please feel free to contact us with any questions or comments.



**Testimony
of
Keith R. Clifford
on behalf of the
Wisconsin Association for Justice
before the
Senate Judiciary, Corrections, Insurance,
Campaign Finance Reform and Housing Committee
Sen. Lena Taylor, Chair
on
2009 Senate Bill 9
February 5, 2009**

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Good afternoon, Senator Taylor and members of the Committee. My name is Keith R. Clifford. I am a partner in the Madison law firm of Clifford and Raihala. I am a past president of the Wisconsin Association for Justice (WAJ) and serve as Chair of the Legislative Committee. I appear on behalf of WAJ in favor of SB 9. Thank you for this opportunity to testify.

From the moment we begin to learn, one common theme is drummed into our minds – it is wrong to lie.

We especially don't like it when someone lies to us when buying a home. For most Wisconsinites it is the single most valuable possession they will ever purchase. This is why the Supreme Court decision in *Below v. Norton*, 2008 WI 77, ___ Wis. 2d ___, 751 N.W.2d 351, was so shocking. In a 4 to 3 decision, the Court limited the punishment for homeowners who lie about the condition of their home.

Below involved the purchase of a home in south Milwaukee by the plaintiff, Shannon Below, from the defendants, Dion and Dana Norton. When the Nortons put the home on the market, they affirmatively represented in the mandatory property condition report that they were unaware of any problems with the home's plumbing system other than a minor problem with a bathtub drain handle. Based on that property condition report, Below ultimately purchased the home. However, after the purchase, Below learned that, contrary to the property condition report, the sewer line running from the home to the street was broken. Below subsequently filed suit against the Nortons, alleging: (1) that the Nortons knew of the defective sewer line before the purchase, but intentionally misrepresented the condition of the home's plumbing system on the property condition report to fraudulently induce her to purchase the home; and (2) that she relied to her pecuniary detriment on this intentional misrepresentation in deciding to purchase the home.

For over a century, this state has allowed injured homeowners to pursue a fraudulent misrepresentation claim in tort against the homeowner who lied about the condition of the home. Now the Supreme Court says that claim no longer exists.

Writing for the dissent, Justice Bradley put it very clearly: "According to the majority, a person selling a home can look the buyer in the eye, lie about the condition of the home and escape legal consequences in tort for the lie because of the economic loss doctrine." Wisconsin has the "dubious distinction" of being the only state in the country to hold that the economic loss doctrine bars claims for fraudulent inducement in residential real estate transactions.

The economic loss doctrine was created by judges to prevent parties to a contract from pursuing a recovery in tort when the damages suffered were economic or commercial losses. Initially it was applied to commercial parties where there was equal bargaining power. The idea behind the economic loss doctrine was to encourage parties to a contract to bargain on how to resolve disputes. In the last 20 years the economic loss doctrine has expanded. As Chief Justice Abrahamson wrote in an earlier case, "Like the ever-expanding, all-consuming alien life form portrayed in the 1958 B-movie classic 'The Blob,' the economic loss doctrine seems to be a swelling globule on the legal landscape of this state. ... At the current pace, the economic loss doctrine may consume much of tort law if left unchecked." With the Court's decision, the economic loss doctrine, once a very narrow doctrine, has been expanded to apply to average homebuyers seeking damages against a seller who lies about his home. We believe this is wrong.

The basic underlying purpose of tort law is to require each of us to act as a reasonable person to prevent harm to another. When a person lies, he violates this basic duty each of us owe one another. That is why the tort of fraudulent misrepresentation was created, to find a remedy for a serious wrong against community values.

Applying the economic loss doctrine to the tort of fraudulent inducement eliminates liability for any pre-contract wrongdoing. Contract law imposes duties of good faith and fair dealing generally only after the contract is in force. In other words, contract law only concerns itself with fraudulent performance – knowingly substituting a lower quality of goods than those called for in the contract – not with fraudulent inducement to enter the contract – knowingly misrepresenting the quality of goods to the buyer to get them to enter into the contract.

In addition, applying the economic loss doctrine to limit tort claims for fraudulent inducement does not protect parties' – be they commercial or private individual consumers – freedom to allocate risk by contract. It is well established that parties cannot allocate liability for intentional misconduct. The lying party would never have any incentive to negotiate fairly since it would defeat the purpose of the lies – to defraud the other party. Contract negotiations that begin with the assumption that the other party is lying do not encourage free and open bargaining. Parties cannot freely allocate risk if they cannot rely on the other party to speak truthfully during the negotiation of the contract since they would not know what is true and what is a lie.

So why does the application of the economic loss doctrine matter in residential real estate cases? Tort and contract claims can mirror one another. However, in many other instances, tort claims have significant advantages over contract claims for the injured purchaser. One is the statutes of limitation.

Contract claims often have an identical, if not a longer, statute of limitations than tort claims. For example, claims for breach of contract have a six-year limitation under Wis. Stat. § 893.43, while claims for intentional misrepresentation have a six-year limitation under Wis. Stat. § 893.93(b). As Justice Bradley points out in her dissent, the statute of limitations for contract generally begins to run the moment the breach of contract occurs, while for tort claims, the statute of limitations generally begins to run only after the injured party discovers or reasonably should discover his or her injury. Hence, contract claims can expire before the injured purchaser even knows he or she is injured, whereas tort claims generally do not share this risk.

Another area is damages. Although both contract claims and tort claims may permit recovery of damages for direct and consequential losses, the potential scope of those damages can significantly differ. In general, potential damages are greater under a tort theory than a contract theory.

As an initial matter, under contract law, compensatory damages "are limited by the concepts of foreseeability and mitigation," whereas under tort law, "the only limitations are those of 'proximate cause' or public policy considerations. In addition, under contract law, compensatory damages can be limited by the contract itself.

Punitive damages are also not available as a remedy for breach of contract in Wisconsin. However, punitive damages are available as a remedy for tort claims "if evidence is submitted showing that the defendant acted maliciously toward the plaintiff or in an intentional disregard of the rights of the plaintiff." Wis. Stat. § 895.043(3).

As Justice Bradley wrote in her dissent, good public policy that recognizes the need for truth in human relationships is no longer recognized by the Wisconsin Supreme Court. This decision is bad for the welfare of Wisconsin consumers and bad for the real estate market which must operate in an environment of trust and honesty.

That is why the Wisconsin Association for Justice urges passage of SB 9, which will remedy this great injustice and make it clear to everyone in Wisconsin that if a homeowner lies when selling a home, he or she will be punished for it.

